CONGRESSIONAL BUDGET OFFICE
U.S. Congress
Washington, DC 20515

Douglas Holtz-Eakin, Director

July 7, 2005

Honorable Jerry Weller
U.S. House of Representatives
Washington, DC 20515

Dear Congressman:

I am responding to your May 19, 2005, letter requesting that CBO analyze H.R. 1041, the Social Security KidSave Accounts Act. We estimate that, if the bill were enacted in 2005, it would result in additional off-budget outlays of about $8 billion a year, or about $83 billion over the 2006-2015 period (see the table below).

Description of Proposal

Under H.R. 1041, the government would create a $2,000 account for each child born in 2006 or later when he or she receives a Social Security number. That initial deposit would come from the Old-Age and Survivors Insurance (OASI) trust fund, an off-budget account. The $2,000 would increase after 2013 in step with Social Security cost-of-living adjustments.

The bill would also permit voluntary contributions of up to $500 a year through age 18, including rollovers from Individual Retirement Accounts of parents or grandparents. The tax treatment of voluntary contributions is not entirely clear, and the Joint Committee on Taxation has not yet analyzed its implications. Therefore, we focus here on the $2,000 automatic deposits.

Many features of KidSave accounts, including investment choices, would resemble those of the Thrift Savings Plan (TSP) for federal employees. If account holders, or their parents or guardians, failed to express a choice, the government would automatically assign them a default mix: 60 percent in a stock index fund (the TSP's C fund), 20 percent in a corporate bond fund (the F fund), and 20 percent in Treasury securities (the G fund).

The holder could withdraw from the KidSave account when he or she became entitled to Social Security benefits. In most cases that means age 62 or later, although some beneficiaries qualify at a younger age—before age 18 as the children of retired, disabled, or deceased workers, or between 18 and 62 as disabled workers. The bill does not stipulate the method of distribution, which might take the form of annuities, periodic withdrawals, or a lump sum. The amount withdrawn would not affect the owner's Social Security benefit.

Under H.R. 1041, the government would recapture $2,000 (or the balance in the account, if less) in five installments when the owner reaches age 30. Those repayments would be credited to the OASI trust fund. The accumulated investment returns would remain in the account.

Estimated Budgetary Impact

About 4 million children are born each year, so crediting each with $2,000 would mean annual government contributions of about $8 billion. That figure would climb gradually with a growing number of births, the immigration of eligible children, and (after 2013) a rising contribution.

ESTIMATED BUDGETARY IMPACT OF H.R. 1041, THE SOCIAL SECURITY KIDSAVE ACCOUNTS ACT

	By Fiscal Year, in Billions of Dollars									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Estimated Budget Authority [a]	6.1	8.2	8.3	8.3	8.4	8.5	8.5	8.6	8.8	9.0
Estimated Outlays [a]	6.1	8.2	8.3	8.3	8.4	8.5	8.5	8.6	8.8	9.0
MEMORANDA										
New Accounts (fiscal year, millions) [b]	3.1	4.1	4.1	4.2	4.2	4.2	4.3	4.3	4.3	4.4
Government Contribution (calendar year) [c]	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,044	2,089

a. Funds would be disbursed from the Old-Age and Survivors Insurance trust fund, which is off-budget.
b. Estimated number of births, plus immigrants under 18 if born in 2006 or later.
c. Indexed to Social Security cost-of living adjustments after 2013.

From an economic standpoint, the most realistic estimate of the government's cost for each $2,000 contribution is about $1,700. That amount is the net present value of a $2,000 "loan," repayable with no interest in 30 to 34 years, assuming that yields on comparable Treasury bonds are about 5.7 percent and that roughly 10 percent of recipients would not repay at all because they qualify for Social Security sometime before age 30. In fact, if the $2,000 contribution were a true loan, the Federal Credit Reform Act of 1990 would require counting it on that basis.

The KidSave transaction, however, lacks essential elements of a loan—namely, a contract and exchange between lender and borrower. Parents already obtain Social Security numbers for their infants and would not have to take any extra step to participate in KidSave, nor would they give up anything of value. And in the program's early years, they would clearly "own" little of the money, even though they could tell the government how to invest it.

Therefore CBO believes that the initial $2,000 deposit should be treated in the budget as funds that are still owned and substantially controlled by the government. Under normal budget rules, the investment of government funds in corporate stocks and bonds is recorded as an outlay, but investments in Treasury securities are not. In the case of the KidSave accounts, however, that approach would break down over time as earnings accrued and holders changed investments; it would become impossible to track where the government's $2,000 was invested. CBO concludes that the only practical method is to record a $2,000 outlay immediately (or about $8 billion a year for each batch of new accounts) and any amounts recaptured three decades later as receipts.

I hope that this information is helpful to you. If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Kathy Ruffing.

Sincerely,

Douglas Holtz-Eakin
Director

cc: Honorable William "Bill" M. Thomas
Chairman
Committee on Ways and Means

Honorable Charles B. Rangel
Ranking Member